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SUBJECT: NEPAL: GARMENT EXPORTS DROP 43 PERCENT, BUT
LOOKING TO OTHER MARKETS

SUMMARY

1. (U) Nepal's ready-made garment exports to the United States declined by 43 percent in the first five months of 2005 following the expiration of the Multi-Fiber Arrangement (MFA). Entrepreneurs within the garment sector attributed the decline to the combined effects of MFA phaseout and the government's lack of effort to enhance the sector's competitiveness in the global market. Foreign direct investment in Nepal's garment sector, however, has more than tripled during Nepal's last fiscal year; this should lessen the impact of MFA phaseout on the garment industry. END SUMMARY.

NEPAL'S GARMENT INDUSTRY FEELING THE MEDIA AND POST-MFA PINCH

2. (U) According to information published by the Garment Association of Nepal (GAN), export statistics showed the steady decline in garment exports that began in 2004 continued in the first five months of 2005. GAN statistics showed that in the first five months of 2005 ready-made garment exports totaled approximately USD 27 million, compared to USD 47.6 million for the same period in 2004. Both garment sector representatives and the media cited the industry's "erosion in competitiveness," particularly in the wake of the garment quota phaseout, as a main reason for the sharp decline in garment exports. GAN President and entrepreneur Kiran Sakhya also cited the international media's hyperbole in reporting on Nepal's Maoist insurgency as a major reason for the decline in orders from abroad, as foreign importers feared garment orders would not reach markets in time. Lamenting the sharp decline, garment industry representatives feared the sector's demise if immediate measures were not taken to boost competitiveness.

3. (U) Following the phaseout of the MFA, half a dozen companies--including three of Nepal's ten largest garment exporting firms--have shut down operations, affecting the jobs of more than 18,000 people. Press reports attributed this trend to larger importers preferring cheaper suppliers like China. According to garment entrepreneurs, no new, substantial orders were coming in from the U.S.; industries were fulfilling standing orders.

FOREIGN INVESTORS ACTIVE IN GARMENT INDUSTRY

4. (U) Despite the decline of Nepal's garment exports, the Nepalese ready-made garment manufacturing industry recorded a substantial inflow and commitment for new foreign direct investment (FDI) during the first four and a half months of 2005. According to statistics by the Department of Industry (DoI), six FDI projects worth USD 2.4 million have been registered during the first ten months of the current fiscal year (July 2004 to July 2005), as compared with FDI projects totaling USD 702,054 the previous fiscal year. Tana Gautam, Director General of the DoI, noted that five of those projects were initiated in the "post-MFA era." DoI data showed that new investments had come in from the EU, China, India, the U.S., Canada, Russia, and South Korea. The largest of the newly registered FDI companies was J and P Apparels, a U.S.-Indian joint venture. Its USD 1.5 million investment had the capacity to manufacture 1.8 million pieces of ready-made garments, according to DoI figures. FDI coming into the garment sector now, officials noted, was primarily targeted for export to the EU, Canadian and Indian markets. "This is a striking shift as compared to the domestic investment that targeted the U.S. market," Rishi Raj Koirala, Director of the DoI, stated. Nepalese garment manufacturers who had focused solely on the U.S. market were experiencing the biggest jolt after MFA expiration, according to both DoI and the GAN.

NEPAL GARMENT SECTOR: STILL HOPING FOR U.S. CONCESSIONS

5. (SBU) According to City Apparels, a private garment manufacturer based in Kathmandu, GAN continued to hope for bilateral U.S. concessions, similar to those granted under

the African Growth Opportunity Act (AGOA), for Nepal's garment industry. Joint Secretary of the Ministry of Industry, Commerce and Supplies Prachanda Man Shrestha predicted that the "shocks" felt by Nepal's garment industry were to be expected "for a couple of years" after the MFA phaseout. Nepal's garment manufacturers who had relied primarily on Indian middlemen rather than establishing direct links with U.S. importers would be closing their factories, he noted. Nepal remained, however, strategically located between two of the world's largest economies, Man Shrestha emphasized.

COMMENT

16. (SBU) Recent statistics indicate that Post's concerns that Nepal's ready-made garment exports to the U.S. would decline sharply after the expiration of the MFA have materialized. However, worries that the newly unemployed could be targeted for Maoist recruitment appear to be ameliorated by the increase in FDI, offsetting the closure of garment factories. The steady rise in FDI inflow into Nepal's garment sector shows that MFA expiration did not necessarily toll a death knell to Nepal's garment industry.
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